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TAGS: [ECON](#) [PGOV](#) [EC](#)  
SUBJECT: UNCERTAINTY SLOWING INVESTMENT BY GUAYAQUIL  
BUSINESS SECTOR

REF: A. QUITO 152

[1](#)B. QUITO 129

Classified By: Consul General Douglas Griffiths for reasons 1.4 (b) and (d)

[1](#)1. (C) SUMMARY: In the face of continued uncertainty about Ecuador's regulatory environment and long-term policies, Guayaquil's business sector is still holding off on the new investment needed to foster growth and employment. Business leaders expect continued underperformance in 2008, considering that current high prices of Ecuadorian exports ought to be driving strong growth. Most believe that the Correa administration is wary of the private sector, but opinions differ as to how damaging the policies have been and what direction the government will take. The private sector is frustrated by delays in building a new regulatory framework and cautious of what may be coming, particularly proposed restrictions on the already inflexible labor market. In the end, for coastal business leaders used to working around government regulations, the administration's failure to define a clear direction for its economic program may do more damage than any actual policies. END SUMMARY.

GUAYAQUIL BUSINESSES BEARISH FOR 2008(  
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[1](#)2. (C) In a round of meetings with Econcouns and Econoff on March 31, prominent Guayaquil business leaders forecast a poor business and investment climate in 2008, despite fairly favorable external conditions. Worldwide prices of most Ecuadorian exports, such as oil, shrimp, tuna and bananas, are high, and Colombia and Peru are expected to post 5-7% growth this year. However, Guayaquil's private sector agreed with bearish IMF estimates for Ecuador that predict about 2.5% annual growth in 2008. Many believe that this is a result of continued uncertainty about the new regulatory framework and the Correa administration's long-term policies.

[1](#)3. (C) Maria Gloria Alarcon, President of the Guayaquil Chamber of Commerce, noted that most local businesses are in a holding pattern until the country approves its new constitution and President Rafael Correa makes his economic agenda clearer. "The new labor laws approved by the Constituent Assembly have a lot of businesses investing in labor-saving machinery to replace workers who will soon become more expensive," she explained. "But they are not really investing to build additional capacity." Her father, Paco Alarcon, separately told the Consul General that his Venezuelan and Columbian partners have cancelled two planned joint ventures due to the political uncertainty. Carlos Andrade, Acting President of Guayaquil's Chamber of

Industries, said that some companies are investing to maintain their core business sectors, but are not expanding into new areas. He added that, ironically, the uncertainty helps protect established companies, as it scares away new entrants.

BELIEVE GOVERNMENT IS WARY OF PRIVATE SECTOR...

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14. (C) Part of the uncertainty that is paralyzing investment stems from difficulties in interpreting the government's approach to the private sector. Guayaquil's business community generally agrees that the new administration has thus far not fostered a good environment for business and investment. However, opinions differed as to just how "anti-business" the administration really is. Some interlocutors were frustrated by the numerous small regulatory changes the government has imposed, which they believe are chipping away at their ability to do business. According to Guillermo Lasso, President of Banco de Guayaquil, the GOE's bank policies are limiting access to credit, especially for the poor. "Banks no longer have access to the nationwide credit report database, so we are operating in the dark and more hesitant to approve new loans," he told Econcouns. "Lowering interest rate caps will also restrict the supply of credit, unless the government orders us to give more loans." Alarcon pointed to changes in the licensing procedures for importers that have made it harder to bring in goods from other countries. "They now have to get additional approvals from the government to import foreign products," she said. She also stated her belief that Correa is using price controls on milk to directly target her dairy products business, although she acknowledged that her company mainly produces value-added products that are not subject to the price controls.

15. (C) While Lasso and Alarcon are convinced the government is implementing measures designed to hamper the private sector, other business leaders offered more favorable assessments of the Correa administration's reforms. For example, Andrade opined that elements of the new tax law are understandable, given the level of tax evasion. While the law was drafted behind closed doors, the government did consult with businesses about implementing the regulations. "However, how the laws are implemented is the key," he continued, referring to the tax law and other changes. Walter Spurrier, Editor of the Weekly Analysis magazine and a well known economic analyst, also felt that the situation was not as bad many believe. "The coming year will not be good, but it will not be cataclysmic either," he said. The local Toyota and Chevrolet dealers told the Consul General that they are having their best year on record in terms of sales volume. Revenues are down after the Correa administration dramatically increased taxes on luxury cars, but mass market cars are selling in record numbers.

...BUT UNSURE OF GOVERNMENT'S LONG-TERM PLANS

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16. (C) The business community in Guayaquil is also divided over the direction Correa will take after the new constitution is approved. Guillermo Lasso predicted that "Correa will swing firmly to the left." Both he and Alarcon expect the president to propose legislation that further discourages investment after approval of the new constitution and the expected national elections in late 2008. On the other hand, the Chamber of Industries believes that Correa is already backing off from some of the proposals from their first year in office. "The government has learned that the price controls are not working, and they are beginning to move away from using them," said Jose Salvador, Executive Director of the Chamber of Industries. Spurrier added that many of the more economically leftist ministers have left the government in recent months. The government's increase in basic welfare payments, the minimum wage and a new program that allows employees to borrow from their retirement accounts have created a consumer boomlet. A housing

developer recently told the Consul General that his new low to middle class housing developments on the outskirts of Guayaquil are netting record sales, while his luxury developments are unsold because the rich are waiting to see what direction the government takes.

#### UNCLEAR WHAT NEW CONSTITUTION WILL BRING

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17. (C) The other factor contributing to the private sector's uncertainty and reluctance to invest is the fact that they still have only vague ideas about the new regulatory environment the Constituent Assembly will create. Although the Assembly has approved a few measures relating to economic matters, they have still only addressed these issues in broad terms. Guayaquil's private sector was only able to offer a few limited examples of what the changes might look like. "I have it on good authority that the new constitution will go after private property. It will stipulate that all property needs to contribute to social welfare, which gives the government a powerful tool to use against businesses," Alarcon said. Indeed, a draft text from the Assembly calls for an economic model of "solidarity," though it is still unclear what exactly that means.

18. (C) However, Pablo Lucio Paredes, a Quito-based economist and delegate to the Constituent Assembly, said that he does not expect extensive changes in economic provisions between the current and new constitutions, arguing that the constitution is not the appropriate tool to implement Correa's economic vision. He did not anticipate any appreciable change to the definition of private property (Septel).

#### ECONOMY WILL CONTINUE TO UNDERPERFORM

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19. (C) COMMENT: The divergence of opinion of Guayaquil's business leaders illustrates just how much uncertainty the government's policies ) particularly the gap between rhetoric and implementation (Reftel A and B) - have created. Guayaquil's business community has decades of experience dealing with (and finding ways around) government regulations. But with no clear definition on even the broad direction of the economic policy, investment and job creation outside of the retail and construction sectors have largely

come to a stand-still, with negative repercussions over the medium and long-term. Given the current high oil prices, Ecuador's economy will probably continue to muddle along for the rest of the year at its current pace. But when Ecuador's neighbors are posting robust growth and only about 25 percent of the country's workforce in the formal sector, just getting by is not good enough.

GRIFFITHS